Questions Raised on Required Clarity of Disclosures in SEC Filings

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Two recent decisions of the Delaware Court of Chancery separated by only two weeks took seemingly contradictory positions regarding the extent to which corporate disclosures must be made clear in proxy statements and other SEC filings. In an order issued on March 7 in *In re Columbia Pipeline Group Stockholder Litigation*, C.A. No. 12152-VCL (Del. Ch. Mar. 7, 2017), the court invoked the business judgment rule under Corwin v. KKR Financial Holdings, 125 A.3d 304 (Del. 2015), to dismiss challenges related to a stockholder-approved merger. In so holding, the court rejected the plaintiffs' position that the stockholder vote was uninformed by virtue of the target corporation's failure to disclose the ownership stake of Goldman, Sachs & Co., financial adviser to the target, in the acquiror. Citing the Court of Chancery's decision in *In re Micromet Shareholders Litigation*, C.A. No. 7197-VCP (Del. Ch. Feb. 29, 2012), the court ruled that Goldman's disclosure of this stake in a 2016 319-page SEC filing on Form 13F was sufficient.

By contrast, in *Vento v. Curry*, C.A. No. 2017-0157-AGB (Del. Ch. Mar. 22, 2017), the court enjoined a vote on the proposed issuance of stock by an acquiror in a stock-for-stock merger on the basis of a disclosure deficiency. Specifically, the joint proxy statement/prospectus, which formed part of the acquiror's registration statement filed on Form S-4, failed to disclose any facts concerning the financing fees to be received by the acquiror's financial adviser in connection with the merger. Although these fees were not directly disclosed, the defendants asserted that stockholders could derive the fees based on the acquiror's public filings. In the registration statement, a table set forth a series of adjustments to the acquiror's balance sheet that would result from the merger's consummation, including a line item of $14.025 million for "financing commitment fees." Roughly 100 pages into a filing on Form 8-K made by the acquiror a few months earlier, an affiliate of the adviser was identified as contributing 40 percent of the total principal amount of the deal's debt financing. Taken together, the defendants argued that a stockholder could "reasonably conclude" that the adviser's affiliate stood to receive 40 percent of $14.025 million, or approximately $5.6 million, in connection with the financing. In rejecting this argument, the court relied on the "buried facts doctrine," under which a "disclosure is inadequate if the disclosed information is 'buried' in the proxy materials," *Weingarden v. Meenan Oil,* C.A. No. 7291 (Del. Ch. Jan. 2, 1985), explaining that "one reasonably would expect that all material facts concerning a financial advisor's potential conflicts of interest would be disclosed in plain English in one place."

A review of the seldom-invoked buried facts doctrine indicates that these decisions are not as inconsistent as they may at first appear. Derived from federal precedent applicable to disclosure obligations arising under securities law, the doctrine was first applied by the Court of Chancery in *Weingarden v. Meenan Oil.* Although it found no issue with the defendants' disclosure of information relating to recently granted stock options on pages 30 and 31 of a proxy statement rather than at the beginning of the proxy, the Weingarden court cited the federal district court for the District of Delaware's decision in Blanchette v. Providence & Worcester , 428 F.Supp. 347 (D. Del. 1977), as an example of the doctrine's intended purpose. In *Blanchette,* the district court held that Providence and Worcester Co.'s description of the scaled voting provisions governing its stock in a prospectus's opening summary and body were misleading. While the company mentioned in a footnote to its financial statements that these voting provisions

had been invalidated, under the buried facts doctrine, this remote disclosure could not remedy other, more readily identifiable disclosures noting the existence of the provisions that omitted this important fact.

In *TCG Securities v. Southern Union*, C.A. No. 11282 (Del. Ch. Jan. 31, 1990), the Court of Chancery provided further color on the buried facts doctrine, clarifying that "whether information is 'buried' is the type of determination not logically susceptible to a bright line test." As such, the court rejected the plaintiff's argument that material disclosures concerning pending litigation could not be disclosed in a proxy statement's footnote. Notably, the court differentiated these disclosures from the disclosure at issue in *Blanchette*, which was made in the penultimate page of a prospectus and "radically changed" very significant information disclosed in its body. Moreover, the *TCG* court determined that these disclosures were also sufficiently made in the body of the company's Form 10-K, which was included as an appendix to the proxy statement and cross-referenced throughout the proxy. Since the disclosures were "adequate in detail and reasonably accessible to an interested shareholder," the preliminary injunction sought by the plaintiff was denied.

The Court of Chancery's 1991 decision in *Cinerama v. Technicolor*, C.A. No. 8358 (Del. Ch. June 24, 1991), aff'd in part, rev'd in part on other grounds sub nom. *Cede & Co v. Technicolor , 634 A.2d 345*(Del. 1993), adopted a similar approach, noting that under the buried facts doctrine, "disclosure is inadequate only if there is a reasonable danger that a shareholder would fail to realize the correlation and overall import of facts interspersed throughout the document." In connection with a tender offer and accompanying Schedule 14D-9, it was alleged that merely disclosing the specific stock holdings of each director committed to a related stock purchase agreement in an exhibit to the Schedule 14D-9 was inadequate. In the court's view, however, referring to the filing's exhibits was "a natural and reasonable response" by stockholders desiring to find out precisely how many shares the agreement covered. Accordingly, the court held that it was not "unduly burdensome to have the shareholders look to exhibits for further information of this kind" and found that there was no breach of the duty of disclosure.

As evidenced by these cases, Delaware law does not require all material information to be prominently featured in each proxy statement or other SEC filing made by a corporation. Indeed, in certain circumstances, it may be sufficient to make material disclosures in relatively obscure places, such as in a footnote of or exhibit to an SEC filing or in a filing previously made by the corporation or some other reporting entity. While there is no bright-line rule on when such disclosure is adequate, these cases suggest that whether a disclosure is "buried" may depend on its significance. For instance, vital information, such as the fact that the scaled voting provisions governing stock being solicited in an exchange offer were recently invalidated, should be conspicuously noted. In this regard, it is also notable that Vento involved the disclosure of a financial advisor's conflicts relating to its financing fees from a transaction it advised on—an area that has been the focus of many following RBC Capital Markets v. Jervis , 129 A.3d 816 (Del. 2015). Conversely, in finding disclosures made in past Form 13Fs sufficient in *Columbia Pipeline* and *Micronet*, the Court of Chancery also recognized that the financial advisor in each case held a greater stake in its client than its client's counterparty, and thus there was no material conflict that needed to be disclosed.

Nevertheless, material disclosures should be made in locations stockholders would reasonably be expected to look for them. With respect to the ownership stakes of financial advisors, *Columbia Pipeline* and *Micromet* indicate that it may be reasonable to expect stockholders to look for this information in the adviser's most recent Form 13F. In the context of fairness opinions, Delaware courts have similarly held that the disclosure of an investment banker's

comparable public company analysis does not need to include the specific inputs for or values derived from each company—so long as the comparable companies are disclosed, stockholders can determine where to turn to find the relevant financial information for each precedent transaction. (See *In re Trulia Shareholder Litigation*, 129 A.3d 884, 905–906 (Del. Ch. 2016).) On the other hand, as exemplified by *Vento,* Delaware law does not expect stockholders to sift through all of a company's past filings without direction.

Given the subjective nature of these inquiries, prudent practitioners should seek to prominently note and explain all material information in the body of SEC filings under an appropriate heading and in any summaries contained therein, especially with respect to information of particular significance. If a filing nevertheless seeks to rely on disclosures made in past or extrinsic filings, it should incorporate the filings by reference, expressly refer stockholders to these filings, and explain what types of information stockholders can glean from them. This is particularly true if a past disclosure upon which reliance is sought was made on a form or under a heading that an investor may not reasonably expect the disclosure to be made in.

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